

DEPARTMENT OF ALCOHOL AND DRUG PROGRAMS

SACRAMENTO, CA 95814-4037

TTY (916) 445-1942

(916) 322-4834



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ADP #96-64

To: County Alcohol and Drug Program Administrators

Subject: Prohibition of Profit on Federal Grants

The purpose of this letter is to clarify statutory/regulatory prohibitions of profit on Federal grants, including the Substance Abuse Prevention and Treatment (SAPT) Block Grant.

With the passing of AB 911, effective August 3, 1995, profit on Federal funds is not allowed, and negotiated rates paid to providers are considered provisional reimbursement that must be adjusted to actual cost. Prior to August 3, 1995, only SAPT Block Grant funds used for the Drug Program (not Alcohol) were exempt from settlement to actual cost if negotiated rates were used as a county's payment methodology. Specific citations are shown below.

FEDERAL BLOCK GRANT REQUIREMENTS

Various SAPT Block Grant requirements deal directly or indirectly with the issue of payment for profit. Typically, the issue of profit has arisen in relation to counties using the "negotiated rate" methodology for payment of providers. Current law requires that SAPT Block Grant funds be used to pay only the actual costs of the services provided. We refer you to the following:

- ! The Grant allows only for payment to nonprofit subrecipients. The fact that for-profit organizations are excluded implies an intent not to allow profit. See Public Law 102-321 (USC 300x), Section 1931(a)(1)(E).
- ! Notwithstanding specific Grant restrictions and other applicable Federal statutes and regulations, the Grant defers to State laws and procedures for obligation and expenditure of Grant funds. See 45 CFR 96.30.
- ! A review of State laws and procedures that would apply to the Grant reveals the following:
 - " There are explicit Health and Safety Code requirements which restrict reimbursement to actual costs.

- ▶ Sections 11818(a) and 11991.2 deal with "...expenditures made by counties and contract providers that may be reimbursed...". The common definition of expenditure is "outlay", indicating that something was spent or paid out. Profit would not logically fall within that definition.

- ▶ Prior to August 3, 1995, Sections 11818(b) and 11987.5 contained the following language:

"The cost of services specified in the county alcohol program plan shall be actual costs as determined with standard accounting practices or a negotiated rate."

However, Section 11987.5(b), which applies to the Drug Program only, contains the following language:

"Once the negotiated rate has been approved by the county, all participating governmental funding sources, except the Medi-Cal program ... shall be bound to that rate as the cost..."

- ▶ Sections 11818(b) and 11987.5 were amended, effective August 3, 1995, to contain the following language:

"...the cost of services specified in the county alcohol (drug) program contract with the department shall be based upon reimbursement of actual cost as determined with standard accounting practices. The county may enter into a contract at the actual cost or a negotiated rate."

and

"For those providers who operate under a negotiated rate for non-Medi-Cal services, the rates shall be treated as provisional rates, subject to year-end settlement to actual costs."

Based on the above State requirements, it appears clear for both alcohol and drug programs that providers are to be paid for actual costs with Federal and State funds, effective August 3, 1995.

For alcohol programs, the Department views negotiated rates as provisional for all fiscal periods, due to the absence of the language binding the funding sources to the negotiated rates approved by the counties.

CENTER FOR SUBSTANCE ABUSE TREATMENT DISCRETIONARY GRANTS

Various types of discretionary grants (i.e., Waiting List Reduction and Critical Populations) have been provided by the Center for Substance Abuse Treatment (CSAT) through ADP. Prior to FY 1993-94, funding was passed from ADP through the counties to providers. Beginning with FY 1993-94, these grants have been subgranted directly from ADP to providers. Key requirements were contained in the grant award document and in the subgrant agreements. One such requirement is the prohibition of profit.

Based on the grant awards, the requirements/restrictions related to profit are as follows:

! 45 CFR, 92.22, states, in part:

"Grant funds may be used only for:

(1) The allowable costs of the grantees, subgrantees, and cost-type contractors, including allowable costs in the form of payments to fixed-price contractors; and

(2) Reasonable fees or profit to cost-type contractors but **not any fee or profit (or other increment above allowable costs) to the grantee or subgrantee.** (emphasis added)

"Contractors", in the context of this regulation, are not grantees or subgrantees, who are accountable for the use of the grant funds. The term "contract", according to 45 CFR 92.3 means "a procurement contract under a grant or subgrant."

! 45 CFR, 92.22, also establishes that allowable costs are to be determined using OMB Circular A-87 for state and local government, and using OMB Circular A-122 for nonprofit organizations. These circulars make no provision for an overall profit as part of allowable cost.

- ! The Public Health Services (PHS) Policy Statement, Appendix 6, deals with grants to for-profit organizations. Except under certain conditions contained therein, the policy is that,

"...no profit or fee will be provided to for-profit organizations through financial assistance awards. A profit or fee is considered to be an amount in excess of actual allowable, allocable, and reasonable direct and indirect costs which are incurred in conducting the assistance project."

The principle here, that even a for-profit contractor is not to make a profit on these Federal funds, should be considered as indicative of the Federal view regarding profit.

We hope this clarifies the issue of profit on Federal funds and how the matter will be viewed during our audits. However, if you have additional questions, please contact me at (916) 322-4834 or Andy Dill at (916) 324-6406.

Sincerely,

GARY BELLAMY, Manager
Audit Services Branch

cc: Wagerman & Associates